MORTGAGE BULLETIN

PUBLISHED IN THE INTERESTS OF REAL ESTATE ANALYST SUBSCRIBERS BY

ROY WENZLICK & CO.

Real Estate Economists, Appraisers and Counselors

MARCH 16 1951

Volume XX

Number 12

"MORTGAGE X RAYS"

THE trouble with housing construction in 1950 was that business was too good. The Housing Act of 1950 jet-propelled the booming volume of residential building to the jumbo figures of 1,112,600 starts at the end of September, and even in the face of the new credit regulations the last three months of the year added another 282,500 to swell total starts for the year to an all-time record of 1,395,100. Single-family houses accounted for an estimated 1,156,000 starts or 83 percent of all new dwelling units put under construction during the year. This tremendous building program was sparked by and, in turn, contributed to, a rapid expansion of mortgage financing. Fanned by easy credit terms, and the fear incentive of impending stricter curbs on home purchases, new loans increased by leaps and bounds, reflecting a mushrooming of new debt faster than previously contracted debt was being repaid. At the end of the third quarter new loans on small construction reached nearly $12 billion . . . an annual rate of approximately $15 billion. This would indicate that after deducting prepayments and satisfactions, the net addition to the home mortgage debt for 1950 is very likely to be $5 billion. According to recent figures of the Department of Commerce the total noncorporate, nonfarm mortgage debt is approximately $56 billion. About 70 percent of this is represented by loans on one- to four-family residential properties and 30 percent by loans on apartment and commercial buildings.

Mortgage financing is a big business and a very necessary and important business under a peacetime economy. Without real estate credit the broad scope of home ownership would be impossible. However, in a time of national emergency a rapid expansion of such credit is an inflationary factor which must be restricted. The alternative to controlling the upward spiraling of currency and credit is either direct regimentation or continued inflation.

It has been clearly evident from the beginning of the Korean conflict that the nation's huge rearmament program could not be successfully superimposed upon a national economy operating at top capacity without a cut-back in civilian production. It has been equally patent that one of the most conspicuous areas for such action was the building industry, with particular emphasis on the segment engaged in home construction. Residential building had been a powerful element in the reinflation of 1949-1950; since its major activating force was a redundance of mortgage credit on superlatively easy terms, it could, in all probability, be deactivated by a strong program of qualitative credit curbs. Hence the authority for such controls was included in the Defense Production Act of 1950 and made effective under Regulation X.

As soon as the Federal Reserve Board and the Housing and Home Finance Agency lowered the boom on mortgage credit there ensued a storm of protests, criticisms

and irresponsible attacks on the Regulation. Builders, real estate men, labor leaders and a few mortgage bankers vociferously condemned the regulations as too drastic or not necessary at all. In recent months there is still some grumbling but the opposition and resentment are outwardly, at least, gradually subsiding, except among a few die-hards who believe that at all costs the herd must be saved -- rumps together, horns out. Rather, now the argument is concerned more with that old theorem of our school days, i. e., that X represents the unknown quantity. In this instance the unknown quantity is the volume of home financing in 1951.

The blueprint for residential building was unrolled when the government announced that the target for housing in 1951 would be about 850, 000 starts. However, Raymond M. Foley, Administrator of the Housing and Home Finance Agency, has repeatedly declared that if the target can remain unchanged, the regulations can change. If production of housing continues unduly large, the restrictions will be tightened. If it falls too far short, they will be liberalized. Mr. Foley said recently that credit controls on private home construction may be relaxed in certain defense areas soon. Only those who are puissantly optimistic expect housing to exceed 850, 000 starts. By far the larger number in the building industry have expressed the opinion that if Regulation X is continued in its present form it may reduce building to about 50 percent of last year's total, and there are some who have conjured up so many hobgoblins that they seemingly are convinced that housing construction won't go above 400, 000 starts.

About 80 percent of those who buy nonfarm homes have to finance their purchases through a mortgage loan. What home buying means to institutional lenders is emphasized by the following data. These statistics, with the exception of housing starts (BLS) are from the Survey of Consumer Finances released by the Board of Governors of the Federal Reserve System.

	Housing starts (nonfarm)	Housing purchases: Total expenditures (in billions)	New units (in millions)	Existing units (in millions)
1947	849, 000	$15.5	0.6	1.6
1948	931, 600	21.3	0.8	1.6
1949	1, 025, 100	11.2	0.6	1.0
1950	1, 395, 100	21.3*	1.9*	0.8*

*Planned purchases. Actual purchases have not as yet been released.

Reverting to Regulation X -- just how big a "bite" the regulations will take out of the mortgage business during 1951 is a question for which no one has an unqualified answer. That it will be a major amputation is not inevitable. Conjectures that it may be are overlooking the important factor of demand by lending institutions in relationship to supply. By and large during the past few years banks have been actively aggressive in seeking mortgage investments. Some of them have a substantial backlog of commitments which may have an effect on their demand for mortgages. As a banker we know says, "mortgage commitments are something like a funnel. You put them into the top and they trickle out gradually, and you always have a backlog at the top of the funnel." It appears reasonable to us that the backlog may affect the mortgage demand by slowing down the potential requirements necessitated by amortization and satisfactions. Other banks have nearly attained

or are speedily approaching their portfolio goal in real estate loans as a percentage of bank assets. We understand banks in this category are increasing. A further factor tied in with a possible diminishing demand for mortgages is the purchase of government bonds in the period ahead for the financing of our huge rearmament.

With some of the large banks in the metropolitan cities the regulations are indubitably a challenge as their investment requirements run into many millions of dollars. The president of a large savings bank in the New York area recently said his bank does not expect to feel the effects of Regulation X until next June or July because of the great number of building loans already committed and houses already started. There is no denying, he adds, that Regulation X requirements for higher down payments and shorter term mortgages have had a tremendous effect on potential building in this area. One year ago his bank was handling $4 million to $5 million a week in building or home mortgage commitments. Today with the same sort of open winter the bank is handling less than $1 million a week, and much of this is to purchase or refinance existing homes. This bank made well over $141 million of home mortgages in 1950 and estimates its volume will shrink to about $100 million during 1951 - a drop of 29 percent. However, despite the regulations, with a strong backlog of commitments already in their portfolios, a higher turn-over in existing houses and new construction in excess of 700,000 units per year, there is reason to believe that many banks and other mortgage lenders will be successful in maintaining a substantial volume of mortgage business during 1951. But with competition on high stilts it means gearing for an aggressive job of getting mortgage loans.

Savings and loan associations, with the possible exception of some large shops in the bigger cities that have been active in FHA loans on multiple housing projects, rather expect the regulations may work to their advantage. Since, as a group, they have relied on conventional mortgages to a somewhat greater extent than have other institutional lenders, savings and loans are likely to harvest a larger share of available residential financing during 1951. Their financing of conventional loans on existing houses is not restricted, and on new construction most of their operations fall into loans on properties in the $10,000 class or less. On these loans the down payment is not heavier than they have required, generally, nor the amortization and maturity out of line with customary practice. Moreover, operating heavily in financing homes in the low priced brackets a major segment of their business is in an area that probably will continue almost as brisk in 1951 as it was in 1950.

Here and there concern is voiced that the government may eventually seek means to curb loans on existing houses. But with no strategic materials involved in the sale of older homes, restrictions are not apt to be imposed on mortgage lending in this field. It wouldn't make sense anyway for the government to intervene with institutional lenders operating under the terms of their charters unless it should develop later that a sharp inflation is taking place in the price of older properties.

Changes are occurring in the pattern of mortgage lending. The revamping and further liberalization of the credit provisions of the Housing Act, particularly in the GI section, where the guarantee was boosted to 60 percent with a maximum of $7,500 under 501b, started a swing from FHA to GI loans. FHA, which up to that time had the lion's share of loans being made, began to lose ground. As an example of the upsurge in GI loans, applications in July were over 60,000, in August 70,000, and in September 65,000, while FHA applications in July were 40 percent less than the all-

time top figure of January 1950, and applications for new one- to four-family units in September tumbled badly. In November FHA applications for new dwelling units fell to a 27-month low of 18,000 units. According to Department of Commerce figures home mortgages insured or guaranteed by the FHA for 1950 total $2,482,037,000; for the VA the total (principal amount) for 1950 is $3,073,309,000.

Since the imposition of Regulation X there has been a mounting appetite for conventional loans. Whether this is significant of a definite trend remains to be seen. Many institutional lenders are in a position to grant as liberal terms as can be had under present FHA regulations: and of course a conventional loan can be made in less time and with far less red tape, and, usually, at less expense than an FHA loan. Among lenders, however, who have placed almost entire reliance on FHA and GI loans by various originating and brokerage sources, there are many who have a lot to learn about mortgage lending by conventional standards.

We know of a number of vigorous savings banks in New England which are making conventional loans and have no interest in insured or guaranteed mortgages on the grounds that they want more favorable earnings. They insure them with general mortgage reserves and rely on their own prudence in evaluating risks, having a firm conviction that the continued deterioration of the dollar will make even a marginal loan safe. In fact, some of these men believe that lenders who lean heavily on government insurance and guarantee of real estate loans are encouraging the government in wielding an increasingly powerful influence over real estate credit.

Home building came through magnificently in January. Preliminary BLS estimates total 87,000 starts, and reports already indicate that February starts may reach an unseasonally high level. The picture took on a brighter aspect with the reported statement by W. A. Clarke, consultant to the office of Real Estate Credit, Federal Reserve System, at the MBA mid-winter conference in Chicago, that "the government target for 850,000 starts in 1951 will stick. And materials will be available for that volume."

In compacting the comments made by mortgage operators I find a unanimity of opinion that the mortgage business will be satisfactory through June but with some dwindling in volume during the last six months of the year; beyond that, "no comment." As a criterion of home mortgage volume in 1951 against the boom year of 1950 a glance at the period 1945-1949 may be enlightening. During these years an average of 2,521,494 mortgages of $20,000 or less were recorded each year. Most of these loans were on homes for not more than four families, including a few home-and-business dwellings. The investment involved in each year's loans was $11,506,990,000.

While making predictions in these parlous times is like inviting ulcers, in the bare bones of a word or two, this observer's "guess" is that $10,800,000,000 will be invested in roughly 1,800,000 home mortgages by the end of 1951.

E. G. Johnson

E. G. JOHNSON